Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms	)	CC Docket No. 98-171
	)	
Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990	)	CC Docket No. 90-571
	)	
Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size	)	CC Docket No. 92-237 NSD File No. L-00-72
	)	
Number Resource Optimization	)	CC Docket No. 99-200
	)	
Telephone Number Portability	)	CC Docket No. 95-116
	)	
Truth-in-Billing and Billing Format	)	CC Docket No. 98-170

COMMENTS ON STAFF STUDY AND REPLY COMMENTS OF
VIRGIN MOBILE USA, LLC

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TABLE OF CONTENTS

PAGE

SUMMARY

Virgin Mobile USA, LLC, ("VMU"), analyzes the validity of the Commission's Staff Study (the "Study") of various Universal Service Fund ("USF") collection proposals and responds to the initial comments on the Commission's proposed reforms to the USF collection methodology, filed February 28, 2003.

VMU believes that while the Study provides useful data for purposes of comparison among alternative contribution methods, the Study contains erroneous assumptions, particularly with respect to wireless service, that lead to erroneous conclusions. The Study therefore understates the adverse impact on consumers of replacement of the current revenue-based contribution system with one of the proposed connection-based collection methods.

The legal rationale for the connection-based proposals is also flawed. Many of the commenting parties that support a change to a connection-based approach ignore the statutory imperative that all entities with interstate telecommunications revenues contribute on an equitable basis to the USF fund. They also would require the Commission to expand the scope of the statutory *de minimis* exemption to the direct contribution obligation. Virtual exemption of interstate interexchange carriers ("IXCs") from the contribution obligation, however, is both inconsistent with the terms of the Act and likely to make the USF program unsustainable by removing the largest category of interstate revenues from the contribution base. Moreover, these proposals would place an excessive contribution burden on wireless consumers and carriers, particularly lower income, low-volume prepaid wireless customers.

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COMMENTS ON STAFF STUDY AND REPLY COMMENTS OF
VIRGIN MOBILE USA, LLC

I. INTRODUCTION

Virgin Mobile USA, LLC, ("VMU"), hereby files its consolidated response to the Commission's Staff Study, released February 27, 2003, analyzing the effects of various Universal Service Fund ("USF") collection proposals (the "Study") and to the initial comments on the Commission's proposed reforms to the USF collection methodology, filed February 28, 2003.

Although the Study provides useful data for comparing alternative contribution methods, certain erroneous assumptions, particularly with respect to wireless service, lead to erroneous conclusions that understate the adverse impact on consumers of replacement of the current revenue-based contribution system with one of the proposed connection-based collection methods addressed by the Study.

The reasoning underlying many comments supporting connection-based collection methods is also flawed. Many of the commenting parties supporting a change to a connection-based approach ignore the statutory imperative that all entities with interstate telecommunications revenues contribute on an equitable basis to the USF fund. They would also require the Commission to unduly expand the scope of the statutory *de minimis* exemption to the direct contribution obligation. Virtually total exemption of interstate interexchange carriers ("IXCs") from the contribution obligation is both inconsistent with the terms of the Act and likely to make the USF program unsustainable by removing the largest category of interstate revenues from the contribution base. Moreover, these proposals would unfairly place an excessive contribution burden on wireless consumers and carriers, particularly lower income, low-volume prepaid wireless customers.

VMU therefore urges the Commission to retain the current system or, if it adopts a connection-based contribution method, to modify the method to make it equitable for wireless consumers as proposed by VMU.

II. THE STUDY HAS FLAWED ASSUMPTIONS AND CONCLUSIONS.

VMU believes that the Study relies on several erroneous assumptions about consumer wireless services, and that as a result, it reaches flawed conclusions. The Study overstates the growth in wireless subscribership, underestimates the number of multiple handset households, and underestimates the increase in prepaid wireless services. Consequently, the Study understates the increase in the USF contributions to be paid by residential customers under the various connection-based proposals. VMU believes that the average household would pay significantly more in USF under the proposed connection-based plans than under the interim plan now in effect. In addition, wireless consumers will likely pay dramatically more in USF as a percentage of interstate revenues. Since the Study fails to calculate the effective percentage rate of contribution to be paid by wireless consumers under the various proposals, it misstates the relative impact on consumers of the alternative proposals. The Study's conclusion that two of the currently proposed connection-based proposals have essentially a neutral impact on the effective contribution levels of consumer customers is flawed.

As VMU recommended in its initial Comments submitted in the Commission's current proceeding regarding reform of the USF collection methodology,[1] the Commission should either reform the connection-based proposals to require "equitable assessment" of all contributing carriers, including revising the definition of "user" for prepaid wireless customers under all proposals, or it should retain the existing revenue-based contribution system.

A. The Study Relies on Several Erroneous Assumptions.

Several of the assumptions that pertain to the growth of the wireless industry underlying the Study are incorrect. They are both overly optimistic about the total growth of the wireless

[1] Comments of Virgin Mobile USA, LLC, CC Docket 96-45, *et al.*, filed Feb. 28, 2003 ("VMU Opening Comments").

industry and too pessimistic about the growth in prepaid services and the number of multiple handset households. As a result , the Study overstates the expected revenue from wireless services and understates the amount of USF contribution that the average household would pay under the various connection-based proposals.

1. The Assumed Total Wireless Growth in the Study Is Too High and Would Lead to Discrimination Against Consumer Customers.

The Study assumes that wireless growth will continue over the next five years.[2] This growth estimate is too high. As the Study correctly notes, there has already been a decline in the growth rate in the industry.[3] While the Study purports to take this trend into account, without explanation, the Study nonetheless assumes a relatively flat growth rate, rather than a continuing decline in the rate of growth in the number of wireless subscribers. Wireless service has been a relatively new entrant into the overall telecommunications marketplace. After twenty years of relatively high growth, the marketplace may be reaching a point of saturation, particularly with respect to interstate business usage. It is thus more likely that growth rates will decline, just as the growth in basic residential wireline services has essentially ended. Wireless service will continue to grow, but at a declining rate.

Overstating the overall rate of growth of wireless services results in a disproportionately high revenue projection in the Study for wireless services relative to the rest of the contribution base; consumers would in fact pay less contribution for wireless services on an average monthly basis under the revenue percentage method than is predicted in the Study. The Study's conclusion that an assessment methodology based on connections, as described in summary

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2 Study, at 14 (using an initial growth rate of 11%).

3 *Id.*

charts two through four, would be comparable in terms of costs to consumers to the revenue-based system is therefore erroneous.[4]

2. *The Study Underestimates Prepaid Wireless Growth as an Overall Component of the Wireless Industry and Thus Would Lead to Discrimination Against Low-Volume, Primarily Intrastate Wireless Consumers.*

The Study underestimates the growth in the subcategory of prepaid wireless services. While it is true that prepaid wireless services have traditionally been a very small portion of the U.S. wireless marketplace, such services are very common in Europe and elsewhere, and they will come to represent an increasing share of the U.S. industry as well. The growth rate of the prepaid sector of the market continues to increase, with several new companies, including VMU, and announcements of entry plans by existing companies (such as Verizon Wireless) having recently increased the visibility of the prepaid sector.

As VMU stated in its Opening Comments in the methodology proceeding, prepaid wireless services tend to have lower revenues per user, lower minutes of use, and lower interstate usage than do postpaid wireless services.[5] Prepaid consumers tend to be younger and have lower income than traditional postpaid consumers. Older consumers may rely on mobile phones only for emergencies, which always constitute local usage. The demographics and usage characteristics of prepaid services suggest that, to the extent that the expected wireless growth is in the prepaid sector, the Study will overstate the expected growth rate for all wireless revenues.

This overly optimistic assumption regarding growth in wireless traffic, leads to an overstatement of the projected average revenue per consumer and the projected revenue growth

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[4] *Id.* at 5-8. In particular, these charts show a nearly identical contribution per household or per subscriber throughout the duration of the Study, with the exception of the "access-transport" methodology. (*See*, Study, at Chart 2.) Significantly, however, all the charts covering the connection-based alternatives show a substantial increase in residential wireless contribution based on handsets.

[5] VMU Opening Comments, at 7.

of the wireless industry as a whole. Given the lower usage patterns of prepaid wireless, an underestimate of the average growth of prepaid wireless overestimates the average growth (or lack of decline) in revenues per subscriber. If a connection-based, rather than a revenue-based system, is implemented, the USF contribution is likely to be a more significant portion of consumer charges. As discussed in VMU's Opening Comments, low-volume, intrastate-only consumers are likely to bear a disproportionate share of the contribution charges if one of the currently-proposed, inequitable connection-based proposals is selected.. These customers are in the weakest position to bear an increase in contribution Only if the current system is retained, or the more equitable connection-based approach recommended by VMU is adopted, can these deleterious effects be avoided.

3. *The Study Underestimates the Future Growth of Multiple Handset Households.*

The Study does not account for the fact that a fast-growing component of the wireless customer base is multiple handset households. The Study assumes a mere 1.6 handsets per household,[6] but many households include two adults with wireless phones, as well ancillary phones for children. Moreover, the study implicitly assumes that all handsets are of equal value—in other words, that the second handset (or third or fourth), will generate the same value as the first handset. This may have been a reasonable assumption for business users, but it is not for consumers.

Services which offer consumers an opportunity to associate numerous handsets with the same billing address and the same "bucket" of minutes typically charge a relatively small amount for the privilege of using the additional handset, including an additional phone number. For instance, a wireless company might receive $35 a month from the core subscriber for a certain

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6 Study, at 6-7.

number of minutes, but the carrier would only receive $5 a month from each additional handset, and that revenue would be for use of the bucket-sharing feature, not for interstate traffic.[7] Because the carrier would not necessarily have an additional sale of minutes (or, particularly, of interstate minutes) associated with the additional handset, the average revenue (and interstate revenue) per handset would drop. (In this particular instance, if all consumer households went from one handset to two, the average revenue per user would decrease from $35 to $20 per month, despite the "growth" of total users.)

Similarly, when a family obtains prepaid wireless service for the household's children, interstate revenue per handset is likely to be below the levels predicted by the Study. Parents use this prepaid service to be able to contact children readily while keeping call expenditures within budgeted amounts. For such users, interstate calls would be rare.

As more ancillary handsets are added to existing accounts or households, the average revenue per handset will decline. Switching to a connection-based regime will therefore cause consumers to bear a much higher percentage of USF contribution as a portion of their total wireless telecommunications expenditures. This will have a particularly deleterious effect on low-volume, less affluent intrastate users.

Further, because much of the usage attributed to the additional handsets is intrastate usage, such as calls between family members or local friends, the current connection-based proposals have a disproportionately adverse effect on multiple-handset residential customers who may make few or no interstate calls with their additional handsets. It seems particularly inappropriate to make families who desire to maintain contact with other family members bear an excessive proportion of USF contributions. Unlike the current system, which limits USF

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[7] *See, e.g.*, website of Sprint PCS, "Second Line to Share" Program, www.sprintpcs.com, which offers a second line for $20, less than 50 percent of the rate for separate phone lines.

contribution to interstate revenues, or the "equitable" connection-based approach recommended by VMU, which requires interstate usage for assessment and focuses on equitable contribution by all industry sectors, the connection-based approaches analyzed for the Study have an adverse, not a neutral, impact on contributions from multi-handset residential consumer customers.

Despite the Study's failures of analysis, the Study nonetheless demonstrates that each of the analyzed connection-based systems would impose a huge increase in contribution per residential wireless handset which would not be matched by a proportionate increase in interstate wireless revenues.

B. The Study Reaches Incorrect Conclusions Concerning the Relative Effects of the Various Proposed Contribution Methodologies.

1. The Three Erroneous Assumptions of the Study Lead to False Conclusions.

Wireless revenues and interstate wireless revenues will likely be lower than predicted, both in real terms and in terms of revenue per subscriber. The projection of the average household contribution to the USF system is also likely to be too low. For comparison purposes, this masks the severe adverse impact of the connection-based approaches on consumers.

While contributions under an interstate revenue-based contribution system accurately track usage patterns, connection-based contribution does not. Contrary to the Study's conclusions, with a change to a flat fee, connection-based collection methodology, USF contribution would become an increasing, not a decreasing, portion of any consumer's telecommunications expenditures. Contributions under a connection-based system would unfairly penalize families for wanting to stay in touch with their children on a local basis. Similarly, excessive USF contribution assessments may become a deterrent to mobile service for low income consumers who would likely make few interstate wireless calls. This does not represent good public policy.

While the Study does not compute the average contribution on a revenue basis, the implicit – but erroneous – conclusion of the Study is clear: consumers will pay roughly the same average contribution under the first and third connection-based proposals as they do under the revenue-based system[8]. This conclusion is wrong. Because the Study overstates the wireless revenues from consumers, and greatly overstates the interstate revenues per handset, the consumer impact of switching to one of the connection-based proposals is inequitable. Under all the connection-based approaches, consumers will pay an increased amount of their total telecommunications expenditures to the USF system and will bear a particularly disproportionate share of total USF contributions, particularly with respect to interstate revenues.

2. The Study Fails to Adequately Compare Effective Contribution Rates.

The Study fails to compare effective contribution to USF per dollar of telecommunications expenditure, much less of interstate expenditure. A detailed analysis would show that the connection-based plans require wireless subscribers to pay increasing percentages to the USF system. While the Study claims to make no conclusions regarding the efficacy of any single collection system, the failure to calculate the connection-based proposals' effective contribution percentages on an interstate revenue basis leaves open the question of how much consumers would effectively pay to the USF system under each such proposal.

USF is not a tax.[9] It is, however, a charge, levied by the government, on services purchased. For the consumer, it contains the primary attributes of a tax. The failure to compare

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[8] Perhaps the Study's greatest value is that, regardless of assumptions made, it clearly demonstrates the disproportionate payments that this proposal will inflict on wireless subscribers. Such a proposal would thus clearly violate the most basic tenet of the USF system: that contributions be equitable among carriers. 47 U.S.C. § 254 (d).

[9] *Texas Office of Pub. Util Counsel v FCC*, 183 F.3d 393, 426-428 (5th Cir. 1999) ("Texas OPUC").

the existing "tax rate" under a revenue system to the effective "tax rate" of the contribution-based systems masks the effective "tax" increase that wireless consumers will face under any contribution-based system. In making a policy decision as to which method to adopt going forward, this "tax" increase must be considered, as must be what is in effect a new interstate USF tax on *intrastate* wireless usage. Policy decisions must be informed by information about the disparate impact of various USF contribution methods on various categories of consumers. Shifting more of the USF burden to consumers, particularly low income, primarily low-volume intrastate users, by switching to a connection-based system, would be analogous to regressive taxation.

C. The Study Demonstrates the Fairness of VMU's "Equitable Contribution" Proposal.

Assuming that the Study's assumptions and conclusions were accurate, the Study's conclusions demonstrate the greater fairness of VMU's proposed equitable contribution system and its sustainability. On an interstate revenue percentage basis, an IXC contribution of two percent of interstate revenues would be essentially equivalent to a wireless contribution of $.30 per handset.[10] According to the Study, in 2002, the total number of wireless connections was 132.2 million. At a proposed fee of one dollar per connection, this would result in $132.2 million in contribution. At $.30 per connection, $39.66 million would be collected from wireless carriers, or $92.54 million less than under a one dollar per connection system. IXCs, on the other hand, had $36.34 *billion* in contribution-base revenue.[11] A mere .25 percent increase in

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[10] VMU Opening Comments, 6-7.

[11] *Id.* VMU reiterates that the IXCs contribute only on interstate revenue. To be equitable, a connection-based system must take into account that only 30 percent (at the most) of wireless revenue that comes from interstate revenue. VMU Opening Comments at 6.

IXC contribution (or a total contribution rate of 1.25 percent) can make-up this shortfall.[12] By 2007, the last year of projections for the Study, an increase in IXC assessment of a mere .60 percent (for a total contribution rate of 1.60 percent) is required to maintain revenue neutrality.[13]

VMU's proposed two percent IXC contribution will thus more than make up this shortfall, while maintaining the Act's requirement to have equitable contribution to the system. (A $.30 per wireless connection assessment is approximately 2.31 percent of wireless interstate revenue,[14] a rough approximation of the two percent IXC contribution recommended by VMU.) Indeed, by raising the IXC contribution, the wireline connection fee can also be reduced.

If the Commission cannot adopt this equitable contribution methodology, then the Study reveals that the Commission must maintain the existing revenue-based system, as recently modified by the interim measures, to avoid violating the Act's requirements of ensuring equitable contribution from interstate carriers.

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12 This figure can be obtained simply by dividing the difference in wireless collection under VMU's plan ($92.54 million) into the total IXC contribution base ($36.34 billion).

13 And, in fact, for the reasons noted above, VMU believes that this number will actually be significantly less, as the projections in the Study overstate wireless growth and IXC revenue declines. Moreover, this calculation assumes that all connection-based contribution rates remain constant, an assumption which of course belies the virtually unfettered increases in contribution rates that have plagued the USF system since its assumption.

14 See VMU Opening Comments at 7. This assumes that wireline service is still assessed at $1.00 per connection. While this would be higher in terms of interstate revenue percentages than the assessments on IXCs and wireless carriers, it could be argued that these services are complementary to the basic wireline service that has 97 percent penetration. The impact on low income users of this assessment is off-set by a lifeline services exemption. Further, because all wireline carriers pass the charge along to customers (and it is readily collectible because it is associated with the basic telephone service), there is an argument that the amount of the charge is equitable to the carriers because it is in fact irrelevant to the local exchange carriers and the assessment provides a base for the fund related to the universal availability of the basic interstate access service capability inherent in the wireline connection. VMU, of course, believes that the current revenue-based approach is the one most equitable to all carriers.

III. THE OPENING COMMENTS FILED BY SUCH INTEREXCHANGE CARRIERS AS AT&T AND MCI CONTAIN NOTABLE MISSTATEMENTS AND OMISSIONS OF BOTH THE FACTS AND THE LAW ON USF CONTRIBUTION.

A. The Claim That There is a Risk of a USF "Death Spiral" Is Erroneous.

A primary argument advanced in favor of any of the three connection-based methodologies is the need to preserve the future of the USF system. Under these arguments, declining telecommunications revenues from IXCs will continue to put pressure on the USF collections and could result in what at least one commenter called a "death spiral," in which a declining revenue base coupled with a continued increase in demands on the system would result in an ever-increasing contribution percentage which would eventually become unsustainable.[15] Even if IXC revenues are declining, they still remain far and away the largest category of interstate telecommunications revenues. Exempting them from contribution is hardly a way to increase the sustainability of the fund.

Some commenters point to the growth of other services, such as VoIP and other Internet-based services, as contributing to the decline in the viability of the USF system and warranting a switch to a connection-based system. This ignores that providers of such services contribute indirectly to USF as end-users of telecommunications services, limiting the potential additional fund support to be derived from this source,[16] even if the Commission decides to expand the base of direct contributors pursuant to the Commission's permissive authority to assess USF on "other providers of telecommunications."[17]

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[15] Comments of AT&T Corp., filed Feb. 28, 2003, "AT&T Comments" at 11-20.

[16] See, Form 499-A, instructions, at 16.

[17] 47 USC 254(d). Such permissive expansion of the contribution base would not require the Commission to first address the larger issue of appropriate regulatory classification of such services.

The claim that growth in wireless services "drain" the USF system is even less supportable. Contrary to the apparent belief of the IXCs, wireless carriers do, in fact, contribute to the USF system under the current methodology. A new service that contributes to USF can hardly be a "drain" on the fund. While the previous safe harbor of 15 percent may have limited the additional funding from wireless service, as VMU agreed in previous filings on the interim collection method revisions, the new safe harbor is at or above industry averages for interstate percentages.[18] The recent increase in the safe harbor to 28.5 percent, along with the new requirement to have carriers report in a unified manner with affiliated carriers, will grow the USF contribution base to reflect virtually all interstate wireless traffic. To the extent that this shortfall is deemed unacceptable, VMU supports the elimination of the safe harbor, except for carriers who can demonstrate an inability to determine actual interstate traffic in a reasonable manner.[19]

The recent changes made in the Commission's interim order have rectified any wireless under-reporting. Further changes, including the shift from a revenue-based system to a connection-based system, do nothing to increase the contribution base; indeed, they only shift the burden from the class of all interstate carriers, as required by the Act, to a mere subset of these carriers.

The proposals advocated by the commenters favoring connection-based plans, in which IXC contributions are either eliminated (numbers plan) or minimized ("minimum contribution" plan), are the greatest threat to the sustainability of the fund. It is not a rational response to the concern that contribution-eligible revenue is declining to endorse a contribution methodology

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18 Ex Parte letter of Diane J. Cornell on behalf of CTIA, filed October 31, 2002, Docket No. 96-95.

19 VMU also supports carrier flexibility in determining interstate usage. Some, facilities-based carriers may be able to determine usage based on cell site usage, whereas other carriers, particularly resellers like VMU, can rely on originating and terminating NXXs to determine interstate usage. Regardless of the method, allocations between interstate and intrastate usage can be made easily and accurately.

that then exempts the largest single component of interstate revenue from contribution. Yet, this result is the obvious outcome of at least two of the three connection-based plans. Under the minimum contribution approach, the interstate revenues of the IXCs contribute at a far lower rate than do interstate wireless revenues.[20] Under the numbers proposal, IXC revenue is exempted completely.[21] It is this exemption (or minimum contribution), and not the alleged shift of IXC revenue to wireless revenue, that is the greatest threat to the survivability of the system. There is no need to place an unfair contribution burden on wireless consumers and carriers in order for the fund to be sustainable.

B. Many Comments Misinterpret the Act's Requirement To Collect USF Equitably.

The Telecommunications Act explicitly requires that the USF system collect from all carriers in an equitable and non-discriminatory manner.[22] VMU agrees with other commenters that the Act does not require strictly equal contribution from contributors, but rather fairness in contribution.[23] However, a system in which every "connection" pays the same amount into the system, is in fact, not equitable.

In reviewing the issue of the Act's equity requirements, the Fifth Circuit concluded, with regard to the assessment of international carriers "...the FCC's interpretation is 'discriminatory' because the agency concedes that its rule damages some international carriers...more than...

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[20] See, VMU Opening Comments at III.A. (describing equitable contribution methodology); see also, Section II.C., *supra* (demonstrating the fairness of the "equitable contribution" proposal using the figures provided in the Study).

[21] See Study, at 8. Virgin also notes that while the "access-transport" proposal does, in fact, collect from IXCs, it does so at the expense of wireless carriers, which would pay double the amount of any other class of carrier, based on the dubious assumption that wireless carriers provide both components as separate services, rather than providing the separate service of mobility, in which access occurs only when there is transport since wireless does not provide users dedicated connections. VMU Opening Comments at 9.

[22] 47 USC 254(d).

[23] AT&T Comments at 38, quoting *Texas OPUC*.

others."[24] The court held that the method through which collection occurs must be reasonably calculated to solicit contributions in an equitable manner from all interstate carriers. The three proposed connection-based systems, however, are *per se* inequitable because uniform connection-based fees have no reasonable relationship to interstate revenues, and special treatment – or exemption – of IXCs is inherently inequitable. Under any of these systems, an IXC with extensive interstate revenue could pay a scant one percent of its interstate revenue into the system (or nothing at all), whereas a wireless carrier could pay seven percent or more of its interstate revenues into the system.[25] No reading of the Act's requirement of "equity" could support such an obvious distortion of the relative interstate revenue collection rates from these carriers.

C. The Comments Similarly Distort the Concept of "*De Minimis*."

Another common misstatement of the requirements of the Act relates to the *de minimis* exemption. AT&T describes the *de minimis* exemption in the Act as exempting carriers from contribution when their contribution is *de minimis* and then posits that it should be assessed only such a *de minimis* contribution.[26] This is circular reasoning, of course, and it grossly misstates the intent of the statute.[27] The Act allows the Commission to exempt carriers whose telecommunications activities are so limited that the contributions would be *de minimis;*[28] in other words, carriers who are *de minimis*. Under no plausible description of *de minimis* could AT&T, the largest IXC in the country, be considered a *de minimis* carrier.

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24 *Texas OPUC* at 435.

25 VMU Opening Comments at 7.

26 AT&T Comments at 40.

27 *Id.*

28 47 U.S.C. § 254(d).

The *de minimis* exemption was clearly not designed for the benefit of large carriers with extensive interstate revenues. Rather, it was intended to provide relief to small carriers whose total revenue is so insignificant that the burdens of USF compliance would outweigh the contribution from these carriers. Moreover, such exempted carriers are deemed "end users" for USF reporting requirements and they therefore pay contributions indirectly.[29] Under the connection-based plans, however, IXCs would be exempted in such a way as to avoid all contribution, both on end user and on wholesale revenue.[30] AT&T has attempted to turn the statutory exemption for truly small carriers on its head, to use it as justification for the exemption to be provided to IXCs under the numbers-based contribution methodology.

This approach exempts significant numbers of interstate carriers (IXCs) from contribution, and it then seeks to justify that exemption on the basis that such exemption of *de minimis* **contribution** is permitted under Act.[31] A connection methodology must seek to collect from all interstate carriers first, and then permissively exempt *de minimis* **carriers** second, and then only from direct carrier, but not indirect end-user, contribution.

D. Further Analysis of the Growth of Demand on the USF System Is a Prerequisite to Overhaul of the Contribution Methodology.

A key component to the sustainability of the system is managing the demand on the USF system. Since its inception, the demands on the USF have continued to grow almost limitlessly. Regardless of whether the cause of this growth is schools and libraries fund increases, or the

[29] FCC Form 499-A, Instructions at 16.

[30] VMU notes that under the minimum contribution plan, wholesale revenue would be counted as end user revenue, which has significant competition-distorting effects. VMU Opening Comments at 12 – 13. In addition to that deleterious result, it does virtually nothing to add to the USF contribution base, as IXCs pay such an insignificant contribution under that plan.

[31] Again, it is *de minimis* **carriers** that are exempt under the Act, not *de minimis* **contributors**.

funding of high cost services such as multiple lines for rural consumers,[32] the continued growth in the demands on the Fund should be studied and reasonable attempts to control it should be implemented. Without reasonable controls on the growth of USF demand, the vulnerability of the Fund may increase and demands on carriers will grow. Eventually, under any contribution methodology, the system could fail of its own weight. Attempts to make major changes in the methodology before addressing the demand issue are premature.

IV. CONCLUSION

VMU acknowledges and applauds the significant effort made by the Commission's Staff to quantitatively analyze the competing USF contribution proposals, but erroneous assumptions result in dubious conclusions. VMU urges the Commission to rethink many of the assumptions and conclusions contained in the Study. The Study has not effectively compared the existing system to the proposals in the terms essential to consumers: the differences in the effective rates of their contributions to the USF system under each proposal, including the differences in the effective contribution rates in terms of percentages of interstate revenues. The Study's implicit conclusion that the competing proposals will result in roughly equivalent contribution by consumers is perhaps the most dangerous, and most erroneous, of its findings.

VMU continues its support of the existing revenue-based system, or, if a move to a connection-based system is deemed necessary now, of VMU's proposed "equitable contribution" connection-based system. The comments filed in support of the previous connection-based methodologies fail to justify such a drastic departure from the requirements of the Act. Although those supporting drastic changes in the USF system assert the changes are necessary because the

[32] *See* testimony of Commissioner Abernathy before Communications Subcommittee of the U.S. Senate Commerce Committee, April 2, 2003 (questioning the need of support for multiple lines in high cost areas).

current system is unsustainable, their proposed connection-based methodologies exacerbate rather than alleviate such sustainability problems through the exemption or under-collection of IXC revenue.

Supporters of the connection-based methodologies tend to distort the applicable standard of equitable contribution. The Act's requirement for equity requires the Commission to select a methodology that will collect from all providers of telecommunications service. equitably It is not sufficient that the system collect equitably from some subset of interstate carriers (those with connections) and not collect at all or on a minimal basis from others. The result is truly a distorted, inequitable system that has not been justified by the comments of its supporters and cannot be rectified to comply with the Act.

The supporters of the connection-based system distort the Act's permissive *de minimis* exemption. The supporters point to this exemption as proof that the Commission has the authority to enact a system that exempts significant numbers of carriers, including, inconceivably, the entire class of IXCs under the numbers-based plan. The only reasonable reading of the Act, however, is that this exemption is meant to cover only those **carriers** who are *de minimis* industry participants, not carriers who have successfully manipulated the USF system to contributions more than *de minimis*. Such statutory gymnastics notwithstanding, the Act's *de minimis* exemption (which is merely permissive) cannot be a meaningful justification for the inequities of the connection-based approaches analyzed by the Study.

The connection-based approaches addressed by the Study are inequitable and contrary to the Act through their exemption of IXCs, are counter to the aims of the USF system by burdening low-income and low-usage users, and possibly make the fund unsustainable as significant portions of total interstate revenues are removed from the contribution base. Absent amending these approaches to render them equitable as applied to wireless carriers and their customers, particularly low-usage customers, the existing revenue-based system must be retained.

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